STANDARD & POOR'S

Global Credit Portal
RatingsDirect®

January 27, 2010

Summary:

Chula Vista, California; Appropriations

Primary Credit Analyst:
Paul Dyson, San Francisco (1) 415-371-5079; paul_dyson@standardandpoors.com

Secondary Credit Analyst:
Timothy Barrett, New York (1) 212-438-6327; timothy_barrett@standardandpoors.com

Table Of Contents

Summary:

Chula Vista, California; Appropriations

Credit Profile		
US$27.54 mil rfdg certs of part ser 2010 due 09/01/2032		
Long Term Rating	A-/Stable	New
Chula Vista approp		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Chula Vista certs of part (Civic Ctr Proj - Phase 2) ser 2006		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Chula Vista certs of part (Police Facility) ser 2002 dtd 06/20/2002 due 06/20/2033		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services assigned its 'A-' long-term rating to Chula Vista, Calif.'s certificates of participation (COPs), series 2010. At the same time, Standard & Poor's affirmed its 'A-' underlying rating (SPUR) on the city's outstanding COPs.

The ratings reflect our opinion of the city's:

- Participation in the San Diego area's broad economic base;
- Above-average income and wealth indicators; and
- Improvement in financial performance after a prolonged trend of deficit spending to sustain what we consider to be good reserve levels; and
- Adoption of an enhanced reserve policy and plans to develop its funding strategy.

The credit strengths are tempered by our opinion of the persistent budget pressures as evidenced by the debt refunding plan and exposure to additional budget pressures if developer fees do not improve in the medium term.

The COPs have an interest in lease payments to be made by the city to the Chula Vista Public Financing Authority for leased assets consisting of the city's corporation yard administration building and fire stations number 4, 6, and 8. Under the lease purchase agreement, the lease is subject to annual appropriation. However, the city has covenanted to budget and appropriate annual lease payments. Additionally, the lease is subject to abatement for damage or destruction, which we believe is mitigated by the city's covenant to maintain rental interruption insurance equal to 24 months of lease payments and casualty insurance for certain loss or damage equal to the replacement cost of the leased assets.

It is our understanding that the COP proceeds will be used to refund the city's series 2000 COPs ($15.6 million) to allow the city to capitalize interest, or defer about $1.1 million of annual interest payments, through fiscal 2014 and extend the final maturity by about 10 years. Additionally, we understand that the city plans to use about $9.4

million in new bond proceeds to provide additional cash flow to meet debt service requirements during the next three fiscal years. However, this will also add an additional $1.38 million of average annual debt service between fiscals 2014 and 2033. Prior to this financing, maximum annual debt service (MADS) on the city's outstanding COPs was about $5.4 million between fiscals 2011 and 2021. Based on the pro forma debt service after the restructuring, MADS is about $5.9 million between fiscals 2014 and 2031. Lease payments on the city's outstanding COPs have been funded with public facility development impact fund revenue (development fees). The city reported that about 700 new residential units per year are required to fully service the debt from developer fees, which declined to about 250 for fiscal 2009, from a peak of about 3,600 in fiscal 2005. Annual total governmental developer fee revenue ranged from $10.6 million to $50.6 million during the peak between fiscals 2000 and 2006, and fell to between $9 million and $24 million during fiscals 2006 and 2009. The city anticipates future development that will yield about 24,200 new units.

Chula Vista is located 8 miles south of San Diego and participates in the San Diego MSA. We believe that the city's proximity to Mexico's border, just 7 miles to the south, also creates an economic link to nearby Tijuana. Major employers in the city include:

- Sweetwater Union High School District (4,435 employees),
- Chula Vista Elementary School District (2,753),
- Southwestern Community College (2,400),
- Rohr DBA Goodrich Aerospace (1903), and
- Sharp Chula Vista Medical Center (1,799).

The city's unemployment rate (not seasonally adjusted) has grown steadily to 11.7% for December 2009 from 3.8% in December 2000. Although a lagging indicator, Chula Vista's median household effective buying income has been increasing since 1998 and reached 122% of the national median for 2008, compared with 100% in 2000. The population grew to 233,108 for 2009, according to the city.

The city experienced rapid growth during the housing boom, with double-digit annual assessed value (AV) growth rates between fiscals 2002 and 2008, with a peak year-over-year growth rate of 20% in fiscal 2006. The housing downturn slowed growth rates to 2.1% for fiscal 2009 and caused an 8% decline for fiscal 2010, resulting in AV of $22.8 billion for fiscal 2010, or what we consider a still very strong $97,862 per capita.

As a result of the slowdown in economic activity, the city began experiencing revenue shortfalls in fiscal 2007 including a drop in development fees, franchise fees and real property transfer fees, as well as a slow down in sales and use taxes. Management attributes the decline in its general fund balance during this period to the contraction in revenues. Although the city's reserves slipped below the city's reserve policy target of maintaining 8% of operating budget as an undesignated fund balance, management has stabilized the reserve at about 6% since fiscal 2007 and has budgeted to maintain a 6% reserve for fiscal 2010. For fiscal 2009, the audited financial statements show an unreserved general fund balance equal to 8.6% of expenditures. Management reported that savings from staff reductions is largely responsible for their ability to maintain the 6% policy reserve, including closing a $20 million budget gap for fiscal 2010. Additional cost-saving measures for fiscal 2010 were furlough programs, elimination or deferral of cost-of-living increases, overtime reductions, and a freeze on nonessential spending.

Chula Vista's management practices are considered "good" under Standard & Poor's Financial Management Assessment (FMA) methodology. We revised the FMA to "good" from "strong" based on our view of the city's inability to maintain its council policy of maintaining an 8% undesignated unreserved general fund balance since fiscal 2007. An FMA of "good" indicates that in our view practices exist in most areas, although not all may be formalized or regularly monitored by governance officials. The city has formal written policies that cover investments, reserves, and debt management, although debt management policies do not address the use of derivative products. Investment results are reviewed quarterly, with quarterly review of actual-to-budget variances for general fund revenues and expenditures. The city utilizes various outside and inside resources to generate budget assumptions, including the University of California-Los Angeles economic forecast and internal housing growth projections. The city engages in multiyear financial planning, with a five-year forecast, and its capital plan covers a period of five years and fully identifies sources and uses of funds. However, the city reported that it did not perform a five-year forecast during fiscal 2009 to focus its resources on closing the budget gap. Management also stated that it plans to enhance the five-year forecast by mid-fiscal 2011 to include pension reform and a funding plan to increase the council's policy reserve to 23% from a currently funded 6%. The city council's formal reserve policy for the general fund, established in 1996, targeted an 8% reserve. The city council revised the policy in November 2009 to include a minimum of a 15% general fund operating reserve, 5% economic contingency reserve, and 3% catastrophic event reserve.

The city's current overall net debt burden is what we consider high at $5,284 per capita and a moderate 5.4% of market value, of which about 15%, or $187 million, is attributable to the city, with overlapping debt accounting for the balance ($1 billion). The city's direct debt includes $7 million of pension obligation bonds, $130.6 million of COPs, about $3 million of other long-term governmental obligations, and $47 million of redevelopment agency debt.

Outlook

The stable outlook reflects our opinion of management's actions to stabilize financial performance that will retain a reserve of at least 6% through fiscal 2010. Additionally, the outlook reflects our view of the council's policy to substantially increase its reserves and management's actions to develop a multiyear financial plan to achieve the new reserve goal and include pension reform. The stability of the rating will largely depend on our view of the city's ability to continue good financial operations, partly evidenced by its ability to maintain good reserve levels.

Related Research

USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

Complete ratings information is available to RatingsDirect on the Global Credit Portal subscribers at www.globalcreditportal.com and RatingsDirect subscribers at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.